Nonprofit Organizations

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New York's Non-Profit Revitalization Act

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The New York Non-Profit Revitalization Act of 2013 (the "Act") was signed into law December 18, 2013, and the bulk of its provisions will take effect July 1, 2014. As we reported in our previous alert on the subject, the goals of this legislative effort were to modernize the law and reduce administrative burdens on nonprofits, as well as to improve governance accountability and oversight.

The following governance features of the Act apply to all nonprofits incorporated in New York.

Conflict of Interest Policy: A conflict of interest policy is now mandatory and must include the following:

- A definition of conflicts;
- Procedures for disclosure to an audit committee, or if no audit committee exists, to the board;
- A requirement that any conflicted person be recused from deliberations and voting on the subject;
- Prohibition against the conflicted person attempting to improperly influence deliberations or voting on the subject;
- Documentation of conflicts situations, including in minutes of any meetings where discussed;
- Special procedures for disclosing and handling related-party transactions, as detailed below;
- Written disclosure of potential conflicts, including involvement with any entity with which the corporation has a relationship and interest in any transaction in which the corporation is a participant, by all directors prior to election and annually thereafter;
- Written disclosures are to be submitted to the secretary, who must provide copies to the chair of the audit committee, or if none exists, the chair of the board.

Whistleblower Policy: A whistleblower policy is now mandatory for a nonprofit that has 20 or more employees and annual revenue in excess of $1 million; it must include the following:

- Procedures for reporting violations or suspected violations of law or corporate policies, including confidentiality of reporting;

- Reporting to a designated officer or employee, who reports to the audit committee or other committee of independent directors or to the board;
- Assurance of no retaliation, including adverse employment consequences, for reporting; and
- Distribution of the policy to officers, directors, employees and volunteers who provide substantial service to the corporation.

Board Independence

- No employee may serve as Chair or hold any other office with similar responsibilities.
- Conflicts or whistleblower deliberations and determinations must be made by a committee (such as an audit committee) or the board, consisting only of "independent directors," meaning directors that are not, and have not in the last three years, been employed by or received more than $10,000 in compensation from the corporation or any affiliate, and have not had a substantial interest in any entity that made payments to or received payments from the corporation or affiliates exceeding the lesser of $25,000 or 2% of the entity's gross revenue, and whose relatives have also been free of such conflicts for the past three years.

Related-Party Transactions

- "Related party" is defined as any director, officer or key employee of the organization or an affiliate, any relative of such individual, and any entity in which any such individual or relative has a 35% or greater ownership or beneficial interest or, in the case of a partnership or professional corporation, a direct or indirect ownership interest in excess of 5%;
- Any director, officer, or key employee with an interest in a related party transaction must disclose in good faith the material facts of the interest to the board or authorized committee;
- Related-party transactions must not only be disclosed but approved by the board as fair, reasonable and in the corporation's best interest;
- No person with an interest in a related-party transaction (including compensation) may be present at or participate in deliberation or voting on it. (The board or committee may request that the person provide information or answer questions prior to the deliberations or voting).

Additional features of the Act apply to charitable nonprofit corporations.

Related-Party Transactions – Augmented Provisions: With respect to any related-party transaction involving a New York charitable nonprofit corporation and in which a related party has a substantial financial interest, the board or an authorized committee of the board must:

- Prior to entering into the transaction, consider alternative transactions to the extent available;
- Approve the transaction by not less than a majority vote of the directors or committee members present at the meeting; and
- Contemporaneously document in writing the basis for the board or authorized committee's approval, including its consideration of any alternative transactions.

Audit Oversight: Charitable nonprofit corporations that are required to register to conduct charitable solicitation in New York (whether or not they are incorporated in New York) may be subject to additional audit oversight provisions. If such a corporation has over $500,000 in annual revenue, it must file an annual audit report with the state, and it must either have an audit committee made up of independent

directors, or have the independent directors on the board serve the function of an audit committee. The audit committee must:

- Oversee the accounting and financial reporting processes of the corporation and the audit of the corporation's financial statements;
- Annually retain an independent auditor to conduct the audit; and
- Review the results of the audit and any related management letter with the independent auditor.

If a corporation that files an annual audit report with New York has over $1 million in annual revenue, the foregoing will apply, and, additionally, the audit committee must:

- Review with the auditor the scope and planning of the audit prior to its commencement;
- Upon completion of the audit, discuss with the auditor any identified material risks and weaknesses in internal controls, any restrictions on the scope of the auditor's activities or access to information, any significant disagreements between the auditor and management, and the adequacy of the corporation's accounting and financial reporting processes;
- Annually consider the performance and independence of the auditor; and
- Report to the board, if the duties detailed above are performed by a committee.

The above governance accountability and oversight changes to New York law should prompt New York nonprofit corporations and other nonprofits registered to conduct charitable solicitations in New York to review their governance documents and procedures.

Additionally, some modernizations to the law may provide new opportunities for New York nonprofit corporations. Modernizations in the Act include explicit allowance for directors and members to conduct business using electronic communications; meeting notices, waivers of notice, proxy voting by members, and unanimous written consents may be communicated electronically (i.e., via fax or email). The Act also explicitly allows for board meetings to be conducted through video equipment in addition to telecommunications equipment. Other provisions of the Act reduce burdens for corporate transactions by requiring only a majority vote of a nonprofit's board or a committee of the board (rather than a 2/3 vote of the entire board) to approve non-substantial real estate transactions, and approval by just the Attorney General rather than a court for a merger or disposition of substantially all of a corporation's assets. New York nonprofit corporations may wish to revise their governance documents and procedures to take advantage of some of these new features in the law.

If you have any questions about the content of this client alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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